

Report of the auditor-general to the Eastern Cape Provincial Legislature and the council on OR Tambo District Municipality

Report on the audit of the consolidated and separate financial statements

Qualified opinion

1. I have audited the consolidated and separate financial statements of the OR Tambo District Municipality set out on pages ... to ..., which comprise the consolidated and separate statement of financial position as at 30 June 2019, the consolidated and separate statement of financial performance, statement of changes in net assets, cash flow statement and the statement of comparison of budget information with actual information for the year then ended, as well as the notes to the consolidated and separate financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the possible effects of the matters described in the basis for qualified opinion section of this auditor's report, the consolidated and separate financial statements present fairly, in all material respects, the financial position of the OR Tambo District Municipality as at 30 June 2019, and financial performance and cash flows for the year then ended in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2013 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act (Act No. 1 of 2018) (Dora).

Basis for qualified opinion

Irregular expenditure

3. The municipality did not fully record irregular expenditure in the notes to the financial statements, as required by section 125(2)(d)(1) of the MFMA. This was due to the expenditure incurred in contravention of the supply chain management (SCM) requirements not being detected and appropriately disclosed in the financial statements. Consequently, I was unable to determine the full extent of the irregular expenditure stated at R1,4 billion (2017-18: R3,2 billion) in note 52 to the consolidated and separate financial statements as it was impracticable to do so.

Property, plant and equipment

4. The municipality did not recognise all items of property, plant and equipment in accordance with GRAP 17, *Property, plant and equipment*. Infrastructure assets that were not completed (Infrastructure WIP) were incorrectly disclosed as completed infrastructure assets and some infrastructure assets that were completed in the prior year were incorrectly disclosed as transfers in the current year. Some of these infrastructure assets were further recorded at incorrect amounts. Consequently, infrastructure assets disclosed in note 9 were overstated and infrastructure WIP was understated by R268,9 million (2017-18: R312,8 million). Additionally, depreciation included in the statement of financial performance was understated and accumulated depreciation disclosed in note 9 to the consolidated and separate financial statements was overstated by R16,4 million.

Commitments – restatement of corresponding amounts

5. In my previous report I modified my opinion on commitments due to the lack of systems and processes in place at the municipality to ensure that commitments are correctly disclosed. A restatement was made to rectify the prior year misstatement, but it could not be substantiated by adequate supporting audit evidence. I was unable to confirm the restatement by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to the commitments corresponding amount stated at R410,8 million in note 41 to the consolidated and separate financial statements.

Context for the opinion

6. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the consolidated and separate financial statements section of this auditor's report.
7. I am independent of the municipality in accordance with sections 290 and 291 of the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* and parts 1 and 3 of the International Ethics Standards Board for Accountants' *International code of ethics for professional accountants (including International Independence Standards)* (IESBA codes) as well as the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA codes.
8. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Emphasis of matters

9. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Bulk water losses

10. As disclosed in note 56 to the consolidated and separate financial statements, material bulk water losses of R11,1 million (2017-18: R21,4 million) were incurred, which represents 31% (2017-18: 47%) of the total bulk water purchased.

Material losses – service debtors

11. As disclosed in note 3 to the consolidated and separate financial statements, material losses of R345,7 million were incurred as a result of a write-off of irrecoverable service debtors.

Corresponding figures

12. As disclosed in note 43 and 44 to the consolidated and separate financial statements, the corresponding figures for 30 June 2018 were restated as a result of errors in the financial statements of the municipality at, and for the year ended, 30 June 2019.

Other matter

13. I draw attention to the matter below. My opinion is not modified in respect of this matter.

Unaudited disclosure notes

14. In terms of section 125(2)(e) of the MFMA, the municipality is required to disclose particulars of non-compliance with the MFMA in the financial statements. This disclosure requirement did not form part of the audit of the consolidated and separate financial statements and, accordingly, I do not express an opinion on it.

Responsibilities of the accounting officer for the financial statements

15. The accounting officer is responsible for the preparation and fair presentation of the consolidated and separate financial statements in accordance with SA Standards of GRAP and the requirements of the MFMA and Dora, and for such internal control as the accounting officer determines is necessary to enable the preparation of the consolidated and separate financial statements that are free from material misstatement, whether due to fraud or error.
16. In preparing the consolidated and separate financial statements, the accounting officer is responsible for assessing the OR Tambo District Municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the appropriate governance structure either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the consolidated and separate financial statements

17. My objectives are to obtain reasonable assurance about whether the consolidated and separate financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these separate financial statements.
18. A further description of my responsibilities for the audit of the consolidated and separate financial statements is included in the annexure to this auditor's report.

Report on the audit of the annual performance report

Introduction and scope

19. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.

20. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.
21. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected development priorities presented in the annual performance report of the municipality for the year ended 30 June 2019:

Development priorities	Pages in the annual performance report
Development priority – KPA 1: Basic service delivery and infrastructure	x – x

22. I performed procedures to determine whether the reported performance information was properly presented and whether performance was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
23. I did not raise any material findings on the usefulness of the reported performance information for this development priority.
24. The material findings in respect of the reliability of the selected development priorities are as follows:

KPA 1: Basic service delivery and infrastructure

Reliability of the reported performance

Percentage of households earning less than R3 200 per month with access to free basic services (P030)

25. I was unable to obtain sufficient appropriate audit evidence to support the reported achievement of this indicator. This was due to inadequate performance management systems and processes that predetermined how the achievement would be measured, monitored and reported. I was unable to confirm the reported achievement of the indicator by alternative means. Consequently, I was unable to determine whether any adjustments were required to the achievement of 65% as reported in the annual performance report.

Other matters

26. I draw attention to the matters below.

Achievement of planned targets

27. Refer to the annual performance report on pages ... to ... for information on the achievement of planned targets for the year. This information should be considered in the context of the material finding on the reliability of the reported performance information in paragraph 25 of this report.

Adjustment of material misstatements

28. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were in the reported performance information of the development priority – KPA 1: Basic service delivery and infrastructure. As management subsequently corrected only some of the misstatements, I raised a material finding on the reliability of the reported performance information. This finding is reported above.

Report on the audit of compliance with legislation

Introduction and scope

29. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.

30. The material findings on compliance with specific matters in key legislations are as follows:

Annual financial statements, performance and annual reports

31. The consolidated and separate financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements of current assets, liabilities, revenue, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected, but the uncorrected material misstatements resulted in the financial statements receiving a qualified audit opinion.

Asset management

32. An adequate management, accounting and information system which accounts for assets was not in place, as required by section 63(2)(a) of the MFMA.

33. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.

Expenditure management

34. Money owed by the municipality was not always paid within 30 days as required by section 65(2)(e) of the MFMA.

35. Reasonable steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA. The expenditure disclosed does not reflect the full extent of the irregular expenditure incurred. Most of the disclosed irregular expenditure was caused by non-compliance with supply chain management (SCM) regulations.
36. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R14,6 million, as disclosed in note 50 to the consolidated and separate annual financial statements, in contravention of section 62(1)(d) of the MFMA. Most of the unauthorised expenditure was caused by overspending on conditional grants.
37. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R967 039, as disclosed in note 51 to the consolidated and separate annual financial statements, in contravention of section 62(1)(d) of the MFMA. Most of the disclosed fruitless and wasteful expenditure was caused by interest paid on overdue accounts.

Procurement and contract management

38. Some of the goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations, in contravention of the SCM regulation 17(a) and (c). Similar non-compliance was reported in the prior year.
39. Some of the goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1).
40. Some of the competitive bids were adjudicated by a bid adjudication committee that was not composed in accordance with SCM regulation 29(2). Similar non-compliance was reported in the prior year.
41. Some of the contracts were awarded to bidders that did not score the highest points in the evaluation process, as required by section 2(1)(f) of Preferential Procurement Policy Framework Act and Preferential Procurement Regulations.
42. Some of the contracts were awarded to bidders based on prequalification criteria that were not stipulated or differed from those stipulated in the original invitation for bidding and quotations, in contravention of the 2017 preferential procurement regulation 4(1) and 4(2). Similar non-compliance was reported in the prior year.
43. The performance of some of the contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA. Similar non-compliance was reported in the prior year.
44. Awards were made to providers who were in the service of other state institutions or whose directors were in the service of other state institutions, in contravention of section 112(j) of the MFMA and SCM regulation 44. Similar awards were identified in the previous year and no effective steps were taken to prevent or combat the abuse of the SCM process, as required by SCM regulation 38(1).

Conditional Grants

45. Performance in respect of programmes funded by the municipal infrastructure grant, regional bulk Infrastructure grant and water services infrastructure grant was not evaluated within two months after the end of the financial year, as required by section 12(5) of Dora.

Other information

46. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report. The other information does not include the consolidated and separate financial statements, the auditor's report and those selected development priorities presented in the annual performance report that have been specifically reported in this auditor's report.
47. My opinion on the consolidated and separate financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
48. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated and separate financial statements and the selected development priorities presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
49. I did not receive the other information prior to the date of this auditor's report. When I do receive and read this information and if I conclude that there is a material misstatement therein, I am required to communicate the matter to those charged with governance and request that the other information be corrected. If the other information is not corrected, I may have to retract this auditor's report and re-issue an amended report as appropriate. However, if it is corrected this will not be necessary.

Internal control deficiencies

50. I considered internal control relevant to my audit of the consolidated and separate financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance on it. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the qualified opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.
51. Leadership has not established an effective compliance- and performance-driven culture within the municipality as evidenced by the number of findings raised during the audit. In this regard, leadership did not appropriately monitor the implementation of policies and procedures to support the achievement of credible reporting and compliance with legislative requirements. Progress on the municipality's audit intervention plan was slow to adequately address issues raised in the previous year.
52. Management did not prepare regular, accurate and complete financial and performance reports that were supported and evidenced by reliable information, as material misstatements

were identified in the annual financial statements and a material finding was raised on the annual performance report.

Other reports

53. I draw attention to the following engagements conducted by various parties that had, or could have, an impact on the matters reported in the municipality's financial statements, reported performance information, compliance with applicable legislation and other related matters. These reports did not form part of my opinion on the consolidated and separate financial statements or my findings on the reported performance information or compliance with legislation.
54. The Hawks are investigating an allegation of the fraudulent appointment of casual workers by the municipality in 2010. The investigation was still in progress at the date of signing this report.

Auditor-General

East London

17 December 2019



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence

Annexure – Auditor-general's responsibility for the audit

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the consolidated and separate financial statements, and the procedures performed on reported performance information for selected development priorities and on the municipality's compliance with respect to the selected subject matters.

Financial statements

2. In addition to my responsibility for the audit of the consolidated and separate financial statements as described in this auditor's report, I also:
 - identify and assess the risks of material misstatement of the consolidated and separate financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control
 - obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control
 - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer
 - conclude on the appropriateness of the accounting officer's use of the going concern basis of accounting in the preparation of the consolidated and separate financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the OR Tambo District Municipality's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the consolidated and separate financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of this auditor's report. However, future events or conditions may cause a municipality to cease operating as a going concern
 - evaluate the overall presentation, structure and content of the consolidated and separate financial statements, including the disclosures, and whether the consolidated and separate financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

Communication with those charged with governance

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.
4. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and, where applicable, related safeguards.